

Fair Political Practices Commission
MEMORANDUM

To: Chairman Getman, Commissioners Downey, Knox, Scott, and Swanson

From: Luisa Menchaca, General Counsel
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Subject: Proposition 34 Regulations, Aggregation of Contributions, Section 85311

Date: September 24, 2001

Introduction

Proposition 34 enacted a new statute governing aggregation of contributions, Section 85311.¹ That statute, in staff's opinion, reinstates the rule in existence between 1976 and 1997, at which point Proposition 208 interposed a very different standard. Believing that Proposition 34 signals a return to the prior rule, and indeed now enacts the Commission's prior regulation implementing that rule, staff suggests that no further regulation is necessary to interpret or apply Section 85311. The bulk of this memorandum describes the evolution of the Commission's prior rule, which culminated in development of the regulation that has become the current statute.

Although the principal focus of this memorandum is construction of Section 85311, a final section takes up the ancillary problem of harmonizing an existing regulation with this new statute. Regulation 18428 governs reporting by "affiliated entities." It is plainly outdated in a few areas, referring to a Proposition 208 regulation no longer in effect, and incorporating language from the predecessor of the current Section 85311. There are also more subtle inconsistencies between Regulation 18428 and Section 85311. Staff will outline the questions raised by Regulation 18428, recommending that the Commission consider amendments in the near future.

Background: Aggregation of Contributions by Affiliated Entities

The Act has always required disclosures relating to campaign contributions, emphasizing information on the sources of these contributions. As shown below, the Commission concluded at a very early date that contributions from two or more persons should be "aggregated" under certain circumstances. When contributions are "aggregated," the contributors are treated as a single person for reporting purposes, and for determining compliance with any contribution limits that might be in effect. The Commission is familiar with a related concept in "money laundering" prosecutions, where one person furnishes money to another on the understanding that the person receiving the money will use it to make a contribution, ostensibly in his own name, thus enabling the first person to evade contribution limits and reporting obligations. Even without actually funding a contribution, if one person effectively

¹ All statutory citations refer to the California Government Code.

dictates the contribution decisions of another, the law requires that their contributions be “aggregated” as the contributions of a single person.

The Commission described the circumstances under which contributions of two or more persons would be aggregated in two 1976 Opinions, *In re Lumsdon*, 2 FPPC Ops. 140, and *In re Kahn*, 2 FPPC Ops. 151. The principles animating these Opinions were applied for more than two decades, until Proposition 208 radically altered the statutory scheme. Prior to Proposition 208, the Commission had shown that the Act required aggregation only in consequence of one person actually exercising control over the contributions made by another. As amended by Proposition 208, Section 85311 spread a much wider net, providing as follows:

“All payments made by a person established, financed, maintained, or controlled by any business entity, labor organization, association, political party, or any other person or group of such persons shall be considered to be made by a single person.”²

It is readily apparent that Proposition 208’s approach to aggregation retained the criterion of control, but also that it introduced additional terms requiring aggregation among parties which simply happened to be related to each other in ways that signaled the *possibility* of control. Thus, for the first time in twenty years, the actual exercise of control was no longer the indispensable criterion for determining which contributions would be aggregated with those of other persons.

Proposition 34 repealed that statute, replacing it with the current Section 85311, which now (after amendment by SB 34, described in footnote 3 below) reads as follows:

- (a) For purposes of the contribution limits of this chapter, the following terms have the following meanings:
 - (1) “Entity” means any person, other than an individual.
 - (2) “Majority owned” means an ownership of more than 50 percent.
- (b) The contributions of an entity whose contributions are directed and controlled by any individual shall be aggregated with contributions made by that individual and any other entity whose contributions are directed and controlled by the same individual.
- (c) If two or more entities make contributions that are directed and controlled by a majority of the same persons, the contributions of those entities shall be aggregated.
- (d) Contributions made by entities that are majority owned by any person shall be aggregated with the contributions of the majority owner and all other entities majority owned by that person, unless those entities act independently in their decisions to make contributions.

² This section was interpreted by former Regulation 18531.1.

This new statute is a verbatim reproduction of former Regulation 18215.1 (a copy of which is included as Attachment A), which had been adopted by the Commission to codify the principles of *Lumsdon* and *Kahn*, but repealed in the wake of Proposition 208.³ The resurrection of this former regulation, serving now as the statute governing aggregation of contributions, marks a return to the *status quo* prevailing before 1997. This was the consensus among those who attended the Interested Persons Meeting held on this subject on August 29, 2001. At this writing, staff sees no basis for a contrary conclusion.

The obvious follow-up question is whether a regulation is necessary to explain the new statute, which itself began life as a regulation explaining when contributions would be aggregated. This question was taken up at the Interested Persons Meeting, and the conclusion was that there is no apparent need for a new regulation at present. This conclusion was based in part on the understanding that the new statute did no more than return the Act to its condition prior to Proposition 208. The fact that the statute is the Commission's former regulation was also a factor which tended to argue against a further regulation.

While the principles of *Lumsdon* and *Kahn* are uncontroversial, there has long been a small but nagging concern over use of the term “directs and controls” to reflect the approach established by these Opinions. The words were first proposed in 1989, for former Regulation 18531.5 (see Attachment B for the language of this regulation as of 1993), carried over in 1995 into Regulation 18215.1, and finally into Section 85311. The Commission may, of course, “interpret” a statute if it contains an ambiguity. If Section 85311 contains *any* ambiguity, it would be found in the term “directs and controls.” However, staff does not believe that these words are unclear, and will argue that any present concern over their meaning arises out of the lingering echo of debates surrounding the adoption of the original regulation, whose initial version generated suspicion that was put to rest by the language eventually adopted, which is the language that survives today in Section 85311.

“Directs and controls:” the Codification of *Lumsdon* and *Kahn*

In *Lumsdon* (Attachment C), the Commission was required to decide whether an individual who was president and majority shareholder of a closed corporation, as well as president of a second corporation and one of three trustees of a foundation owning all the stock of that second corporation was, together with the two corporations and the foundation, a “combination of persons” constituting a “committee” as defined by the then-current version of Section 82013, which provided in pertinent part that:

“Committee means any person or combination of persons who directly or indirectly receives contributions or makes expenditures or contributions for the purpose of influencing or attempting to influence the

³ SB 34 recently introduced an apparently nonsubstantive amendment to subdivision (a)(2), deleting the words “direct or indirect” originally modifying the noun “ownership” in the former regulation and in Proposition 34.

action of the voters for or against the nomination or election of one or more candidates, or the passage or defeat of any measure...”

Relying on the Act’s definition of “person” at Section 82047, together with dictionary and case-law definitions of “combination,” the Commission concluded that the Act’s definition of “committee” referred to:

“[A]n alliance of persons or entities formed for the purpose of influencing the voters for or against the nomination or election of one or more candidates or the passage or defeat of one or more measures. In addition, we conclude that the necessary alliance can be evidenced by an agreement or mutual understanding which can be implied or expressed.” (*In re Lumsdon, supra*, 2 FPPC Ops. at 143.)

Because the majority shareholder of a closed corporation normally exercises almost complete control over the activities of the corporation, the Commission *presumed* that the majority shareholder in *Lumsdon* controlled the contribution decisions of the closed corporation, along with all other decisions of the corporation. The majority shareholder and the closed corporation were thus a “combination of persons” within the meaning of Section 82013, and therefore a “committee.” This presumed affiliation warranted aggregation with the majority shareholder of contributions ostensibly made by the corporation, and this presumption would be “inapplicable only if it is clear from the surrounding circumstances that [the majority shareholder] and [the corporation] acted completely independently of each other.” (*Id.* at 143.)⁴

In *Kahn* (Attachment D), the Commission applied the same logic to presume that a parent corporation controlled the contribution decisions of its subsidiaries. But as in *Lumsdon*, the Commission recognized that aggregation would not follow when it could be demonstrated that parent and subsidiary acted “completely independently of each other” in their contribution decisions.

In *Kahn*, the directors of the parent and subsidiary were largely the same individuals, yet day-to-day decisions for the subsidiary were not made by the directors, but by officers of the subsidiary, most of whom were not directors of either corporation. In particular, officers of the subsidiary made all contribution decisions, acting with discretion in the interest of the subsidiary, without consulting or involving the directors. The only intervention by the directors, it appears, was their establishment of a ceiling beyond which the officers could not authorize expenditures, including campaign contributions, without clearance from the directors. However, contributions made by the subsidiary were apparently always well below that ceiling, and the directors were accordingly never consulted on contribution decisions.

⁴ On the other hand, since the president of a corporation, who was only one of three trustees holding the stock, would normally exercise less control over corporate decisionmaking than would a majority shareholder, the Commission did *not* presume that this individual formed a “combination of persons” with the second corporation.

With these facts in mind, the Commission concluded that the parties before it were *not* a “combination of persons” whose contributions must be aggregated, because in fact the parties had “acted completely independently of each other” in making the contribution decisions. (*Kahn, supra*, 2 FPPC Ops. at 155-156.)

There seems to be no serious question about the core principle articulated in *Lumsdon* and *Kahn*, that contributions should be aggregated whenever one person actually exercises control over the contribution decisions of a second person. Presumptions of such control are permissible in appropriate cases, but such presumptions are always rebuttable by a showing that the person presumably under “control” in fact acted independently in making its contribution decisions.

Neither Opinion employed the compound term “directs and controls,” although cognate words are juxtaposed in *Lumsdon* as follows:

“By definition a majority shareholder exercises almost complete control... He appoints the board of directors and the officers of the company and they are subject to his ultimate direction...”⁵

Lumsdon and *Kahn* treated contributions that would be aggregated for reporting purposes. In 1988, Proposition 73 introduced contribution limits, thereby heightening the significance of aggregation rules which would now act to limit the contributions of “affiliated entities.” In 1989 a new regulation was proposed, expressly to “codify” the principles established by *Lumsdon* and *Kahn*. The initial draft of Regulation 18531.5 called for aggregation of contributions whenever one person “directs, controls, or approves...” the contribution decisions of another. The last word was criticized as an unwarranted extension of the Commission’s prior Opinions. It was soon conceded that the word “approves” implied far less active “control” than contemplated by *Lumsdon* and *Kahn*, and it was omitted from subsequent drafts of the proposed regulation.

Attention next focused on the remaining words. Since “directs” and “controls” were now linked by the disjunctive “or,” the rule of statutory construction disfavoring redundancies in a statute or regulation implied to some observers that these words should have *different* meanings. “Controls” could be limited to mere decisionmaking authority, if “directs” were read to indicate the exercise of that authority. “Direction” (in this sense) was required under the Commission’s Opinions but, linked only by the disjunctive, the proposed regulation suggested that now mere authority, the *potential* for exercising control, was enough to require aggregation. This would have marked a dramatic departure from what the Commission had said in *Lumsdon* and *Kahn*.⁶

⁵ *Lumsdon, supra*, 2 FPPC Ops. at 143.

⁶ These concerns are well summarized in comment letters to the Commission written by Judith S. Davis on June 1, 1989 and Robert E. Leidigh on June 2, 1989.

To avoid any such construction, staff accepted the suggestion made in the letters identified in note 5 above, that the two words be linked by a conjunction. The Commission thus adopted Regulation 18531.5 in a form prescribing aggregation when one person “directs *and* controls” the contributions of another. This language was carried over to the 1995 regulations reproduced in Attachment A, Regulation 18225.4, governing aggregation of independent expenditures, and Regulation 18215.1, repealed with the passage of Proposition 208 and now “re-enacted” as Section 85311. The OAL notice of December 30, 1994, summarized the latter regulation as follows: “The proposed regulation codifies the Commission Opinions, Kahn (1976) 2 FPPC Ops. 151 and Lumsdon (1976) 2 FPPC Ops. 140 regarding aggregation of contributions.”

The meaning and application of regulations 18531.5 and 18215.1 has been well understood since 1989. Any semantic distinction between “direct” and “control” became irrelevant once it was made clear, by joining the two terms with a conjunction, that both were required for aggregation and that, taken together, these terms codified the rule of *Lumsdon* and *Kahn*, that aggregation followed the *actual exercise of control*.

Past Advice Letters, particularly those written before 1989, have on occasion inaccurately referred to the Commission’s aggregation standard as “directs *or* controls.”⁷ However, none of these letters betray any hint of perceived distinction between the two words, and the analysis has always been unaffected by variations in terminology. These letters actually suggest that, to the extent that the authors thought in terms of separate words instead of a single compound, they regarded the two words as synonymous.⁸ No such problem has been detected in letters written after the adoption of the 1989 regulations.

Decision One: Is a Regulation Necessary to Interpret or Explain Section 85311?

Staff has concluded that Section 85311 is free from patent ambiguity, and contains a latent ambiguity only insofar as persons who recall preliminary drafts of former Regulation 18531.5 retain an abiding suspicion that the compound term “directs and controls” is susceptible to misconstruction. The concern that “direct” and “control” are not synonymous words, *and* that they might be applied separately to include conduct not involving the actual exercise of control, is not justified either by the plain language of the statute or by the Commission’s interpretation of the crucial words over the twelve years preceding enactment of the present statute.⁹

⁷ See, e.g. *Lowell* Advice Letter, No. A-85-262; *Walsh* Advice Letter, No. I-88-139.

⁸ The constructional canon that presumes the absence of redundancy in statutes, like all such canons, is a reliable guide only in cases where other evidence points in the same direction. The presence of pleonasms in the law is notorious, illustrated by such well known combinations as “aid and abet,” “cease and desist,” “give and bequeath,” “have and hold,” or “null and void.” Because staff applied the *same* analysis whether the standard was expressed in conjunctive or disjunctive form, these “Freudian slips” indicate that a single criterion was understood, however it might be phrased.

⁹ If it were necessary to assign distinct meanings to “directs” and “controls,” then the statute’s use of the conjunction makes it clear that aggregation is permissible only in those cases where a contribution is “directed” *as*

If the Commission concurs in the judgment that there is no substantial uncertainty as to the meaning of Section 85311, there should be no need to adopt a new regulation to elaborate on a statute that itself began life as a regulation fashioned by the Commission to serve the same purpose. At present, there is little evidence of need for a new regulation. If the Commission interprets Section 85311 differently, or believes that it should be explained in a new regulation, staff will present appropriate language for prenotice discussion at the November meeting.

Decision Two: Whether to Amend Regulation 18428

Regulation 18428 governs the reporting obligations of “affiliated entities.” Its first two subdivisions currently provide that:

“(a) The combined activities of affiliated entities (see 2 Cal. Code Regs. 18531.1) shall be used to determine whether a monetary threshold in the Political Reform Act or these regulations has been met or exceeded.

(b) Affiliated entities which do not receive campaign contributions shall file one campaign statement reflecting their combined activities. The campaign statement shall be filed in the name of the person who **established, finances, maintains, or** controls the affiliate or affiliates, with an indication that the campaign statement includes the activity of these entities. The campaign statements must indicate which entity made each itemized payment. The committee shall identify on its next campaign statement the addition or deletion of any entity with which it becomes affiliated or with which it ceases to be affiliated.” (*Emphasis added.*)

In subdivision (a) the reference to Regulation 18531.1, which implemented the aggregation provisions of Proposition 208, is outdated. Regulation 18531.1 has been repealed and reference to it here should be deleted. In its place, staff recommends reference to Section 85311, governing the contributions of “affiliated entities,” and to 2 Cal. Code Regs. 18225.4, which similarly provides for aggregation of their independent expenditures.

Subdivision (b) imposes a reporting obligation couched partly in the language of the statute enacted by Proposition 208, and since repealed by Proposition 34. The words outlined in boldface type reflect language peculiar to Proposition 208, which might now be deleted from Regulation 18428 as lacking statutory authority. The language remaining after deletion of the four words in bold more

well as “controlled.” The Commission may also conclude that “directs and controls” is better regarded as a pleonasm, a formula where each word fully expresses the meaning of the compound term. In either case, the outcome is the same.

closely tracks the language of Section 85311 and Regulation 18225.4.¹⁰ To *precisely* reflect this language, it would be necessary both to delete the four words left over from Proposition 208 and to insert the words “directs and” before “controls” in the fourth line of subdivision (b), to indicate that the standard of “affiliation” for reporting purposes is the same as the standard used for aggregating contributions in Section 85311, and independent expenditures in Regulation 18225.4. Finally, insertion of the words “expenditures of the” following the word “controls” would bring this regulation more fully into line with *Lumsdon* and *Kahn*. After all this, the second sentence of subdivision (b) would read as follows:

“The campaign statement shall be filed in the name of the person who directs and controls the expenditures of the affiliate or affiliates, with an indication that the campaign statement includes the activity of these entities.”

This reporting regulation may not be a “Proposition 34 issue” at all. But Proposition 34 has effectively redefined “affiliated entities,” at least insofar as they are characterized for purposes of contribution limits in Section 85311. It is arguable that Section 85311, whose scope is confined to certain parts of Chapter 5, does not require changes to a regulation implementing provisions of Chapter 4. To facilitate compliance, staff would prefer that aggregation rules governing contributions and independent expenditures be the same as corresponding rules that define the reporting obligations of affiliated entities, but the Act does not *require* that these rules be consistent for all purposes.

If the Commission will provide its guidance on the appropriate relationship between reporting regulations implementing Chapter 4, and substantive provisions elsewhere in the Act, staff can return with proposed amendments effecting a “technical cleanup” of Regulation 18428 and, if the Commission so decides, with further amendments bringing that regulation into line with the rules for aggregation of contributions and independent expenditures.

Attachments:

- A – 1995 Regulations 18215.1 and 18225.4
- B – Regulation 18531.5 (as amended in 1993)
- C – Lumsdon Opinion
- D – Kahn Opinion

¹⁰ The definition of “majority owned” in Regulation 18225.4(a)(2) is no longer identical to the definition given in Section 85311(a)(2) after SB 34 amended the latter to delete the words “direct or indirect.” In line with the text discussion, the Commission may also wish to consider amending Regulation 18225.4(a)(2) to track the corresponding language of Section 85311.